Supreme Court, U.S.
FILED
OCT 13 1993
OFFICE OF THE CLERK

No. 93-332

IN THE
Supreme Court of the United States
OCTOBER TERM, 1993

MICHIGAN MUNICIPAL COOPERATIVE GROUP and
THE STATE OF MICHIGAN,
Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION and
MIDLAND COGENERATION VENTURE, L.P.,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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BRIEF OF THE MICHIGAN MUNICIPAL LEAGUE AS *AMICUS CURIAE* IN SUPPORT OF THE PETITIONERS

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September 30, 1993

WILSON ✦ EPES PRINTING CO., INC. - 789-0096 WASHINGTON, D.C. 20001

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BRIEF OF THE MICHIGAN MUNICIPAL LEAGUE AS *AMICUS CURIAE* IN SUPPORT OF THE PETITIONERS

The Michigan Municipal League ("League"), pursuant to Rule 37 of the Rules of the Supreme Court of the United States, hereby submits this brief as *amicus curiae,* in support of the "Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit," filed on August 31, 1993, by Michigan Municipal Cooperative Group and the State of Michigan (the "Petition for Certiorari").[1]

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[1] Letters of consent from the parties below are being filed with the Court simultaneously with the filing of this *amicus* brief.

AUTHORITIES INVOLVED

The authorities involved are set out at page two of the Petition for Certiorari and in its Statutory Appendix.

INTEREST OF THE MICHIGAN MUNICIPAL LEAGUE

The Michigan Municipal League is the association for cities and villages in Michigan. Five hundred nine communities are members of the League, and its member communities represent over 98 percent of Michigan's urban population. The League was formed in 1899 and works to strengthen local government and to represent its interests in a variety of fora, including matters before the courts that may have significant impacts on municipalities, their businesses and residents.

Among the interests of the communities in the League are the cost of electricity and the ability of regulatory agencies to effectively regulate the rates charged municipalities, their businesses and residents for electricity. The orders of the Federal Energy Regulatory Commission ("Commission") impair both federal regulation of electricity at the wholesale level and state regulation of electricity at the retail level. As a result, all residents and businesses of the communities represented by the League, whether those communities are served by private utilities, such as Consumers Power Company, or by municipally-owned utilities, such as the utilities comprising the Petitioner Michigan Municipal Cooperative Group, are affected by the decisions of the Commission.

The interest of the cities and villages in the League in electricity costs also drives their concern about the availability in wholesale power markets of the lowest cost electricity possible. League members who own their own municipal electric systems want to purchase low-cost electricity in these wholesale markets. League members who are served by private utilities are similarly affected by whether low-cost electricity is available in such wholesale

markets. Fair competition in these markets will tend to keep costs and rates lower for all electricity users.

The communities represented by the League have a direct interest in ensuring that electricity costs remain reasonably priced for the well-being of their municipalities, their businesses and residents. Because the Commission's decisions adversely affect this interest, the League respectfully submits this brief.

STATEMENT OF THE CASE

The Michigan Municipal League adopts the statement in the Petition for Certiorari.

REASONS FOR GRANTING THE WRIT

This case merits the Court's review because the Federal Energy Regulatory Commission's orders will cause hundreds of millions, if not billions, of dollars in excessive electricity costs to Michigan consumers. As a result of the Commission's orders, ratepayers in Michigan will pay excessive rates for power purchased by Consumers Power Company from its Midland Cogeneration Venture ("MCV") affiliate. But for the interaffiliate, non-arm's-length transactions arranged by Consumers Power, and ignored by the Commission below, Consumers Power could have built its MCV project for one-third to one-half of its $2.3 billion cost. At a time when Michigan's cities and villages are reeling from budget constraints affecting their abilities to meet public needs for essential services, such as public health and safety, the Commission's orders will have adverse economic impacts on every Michigan community. Moreover, the case has important national implications, because of the Commission's refusal to defer to findings of a state agency, which were upheld upon appeal, and because of the anticompetitive consequences of permitting utilities to purchase power from their affiliates.

Michigan's cities and villages are adversely affected in multiple ways. First, the costs to municipally-owned electric systems of providing service will increase. There are twenty-eight such systems in Michigan's Lower Peninsula, serving approximately 1.4 million residents with electric power or street lighting, or both. Their cost of providing service will increase because of the unnecessarily increased cost of power which may be purchased from Consumers Power Company (and indirectly from MCV, Consumers Power's affiliate). Their cost of providing service will also increase because of the incentives created for Consumers Power to use its monopoly control over the electric transmission network and over wholesale and retail electric markets to distort the competitive marketplace for economical alternative sources of electricity. Consumers Power has every incentive to use its monopoly power to protect the market for power from its high-priced MCV affiliate.

Second, those cities and villages served not by municipal electric systems but by privately-owned utilities will experience increased costs from higher rates paid to the private utilities, such as Consumers Power. As the Petitioners pointed out, the record below suggests that in Michigan alone the rate impact of the Commission's orders could be on the order of four billion dollars. This stems from Consumers Power's passing through to its customers the inflated price of its purchases from its MCV affiliate. In addition, Consumers Power's actions with regard to MCV through power exchange agreements increase the costs of Michigan's other major private utility, Detroit Edison Company, thus putting upward pressure on the rates paid by the communities that company serves.[2]

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[2] Consumers Power and Detroit Edison buy and sell electricity from each other through an electric power pool to try to obtain the lowest cost electricity possible to serve the combined needs of their customers. If the cost of MCV's electricity increases and if Consumers Power has incentives to purchase electricity from MCV,

Third, the excessive electricity costs will unnecessarily increase the costs to all cities and villages of providing services to meet basic and vital public needs. Electricity costs are a significant element in the costs of municipal functions, such as the operating costs of water and wastewater (sewer) systems. Electricity costs are the primary cost in lighting city streets, and electricity costs contribute substantially to the cost of lighting, heating and cooling of public buildings. Clearly, electricity is a major item in any city or village budget.

Fourth, in an increasingly tough and competitive global economy, excessive electricity costs also impose burdens on needed economic development throughout Michigan by raising the costs to industries and businesses. This affects not only industries already located in Michigan but also those considering locating or expanding in the state. Michigan's economy continues to be heavily reliant on manufacturing. Unnecessarily high electricity costs place an economic burden on all residents and businesses in Michigan.

The adverse consequences of the Commission's orders are not limited to consumers and businesses in Michigan. The Commission's effective deregulation of rates from cogeneration power plants owned by utility affiliates invites copy-cat projects nationwide, with corresponding proliferation of excessive electricity costs measured potentially in the tens or more of billions of dollars. Furthermore, utilities will have incentives to favor purchases from their affiliates instead of from independent sellers. The anticompetitive consequences of such actions, including upward pressure on rates, along with the incentives for utilities to set up such affiliates to avoid regulation,

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even though less expensive electricity is available from other sources, both Detroit Edison's and Consumers Power's cost of electricity increases. This imposes unnecessary burdens on the municipalities, their businesses and residents who must purchase electricity from these companies.

greatly impair regulation designed to protect consumers against excessive rates.

The Commission's actions improperly interfere with the ability of the Michigan Public Service Commission and comparable state regulatory agencies nationwide to regulate electric rates effectively. The existing monopoly structure of the electric utility industry requires effective regulation. *Gulf States Utils. Co. v. FPC*, 411 U.S. 747, 758-59 (1973). By ignoring the restrictions on utility ownership of qualifying facilities under the Public Utility Regulatory Policies Act (PURPA), 16 U.S.C. § 796(18)(B)(ii) (1988), the Commission has created a loophole that will defeat cost-based regulation by either the states or the Commission of cogeneration power plants owned by utility affiliates, contrary to the purposes of PURPA and to the basic tenets of federalism.

The Commission also improperly disregarded findings by the Michigan Public Service Commission as to the identity of interests between Consumers Power Company and its supposedly independent MCV affiliate. *See, e.g., Consumers Power Co.*, 112 PUR 4th 241, 256 (Mich. PSC 1990). Inexplicably, in erroneously concluding that MCV qualified for a PURPA exemption from state and federal regulation, the Commission ignored these reasoned Michigan Public Service Commission decisions, which were upheld and echoed by the Michigan Court of Appeals. *See, e.g., CMS Energy Corp. v. Attorney General*, 190 Mich. App. 220, 232, 475 N.W.2d 451, 456, *leave denied*, 437 Mich. 918 (1991). Such total disregard of state regulation—and of state agency decisions—warrants review by this Court. *See University of Tennessee v. Elliott*, 478 U.S. 788, 798 (1986). Moreover, the Commission's disregard of the state decisions, contrary to established doctrines of deference, res judicata and collateral estoppel, affects not only Michigan but also implicates the relationship between federal agencies and state agencies across the nation.

The non-arm's-length affiliate transactions, which the Commission's decisions sanction, were used by Consumers Power to improperly inflate the "costs" of the MCV power plant and thus to mask Consumers Power's actual profits from (and ownership share of) its MCV affiliate.[3] MCV's "costs" were unnecessarily inflated to the benefit of Consumers Power by MCV's paying $1.2 to $1.5 billion to Consumers Power for essentially worthless assets from Consumers Power's abandoned Midland nuclear power plant. The uselessness of the nuclear plant assets is demonstrated by the fact that MCV, having spent $1.2 billion for the assets, then spent more to complete the plant (an additional $1.1 billion, for a total "cost" of $2.3 billion) than it should have cost to build the plant from scratch. A similar gas-fired generating plant could have been built by Consumers Power or any number of other private companies without the nuclear plant assets for about $800 million, i.e., for one-third to one-half the "cost" of the MCV plant. The difference—plus some—is what Consumers Power is charging its customers in excessive rates. Building the MCV gas-fired plant with nuclear plant assets was about as cost-effective as converting a space shuttle into a Boeing 737—it can be done, but it is much cheaper to just build a 737. Whatever happens, passengers (and whole states) should not pay high fares for decades based upon grossly uneconomic conversions.[4]

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[3] By masking Consumers Power's profits, MCV sought to support its position that it was not more than 50% owned by a utility, Consumers Power, as required by the Commission's regulations, 18 C.F.R. § 292.206(b) (1993), attempting to implement PURPA's prohibition of utility ownership of qualifying facilities. 16 U.S.C. § 796(18)(B)(ii). The Commission's measures of ownership include looking at the percentage of profits that go to the utility. *Ultrapower 3*, 27 FERC ¶ 61,094 (1984).

[4] Consumers Power went further still and attempted to transfer to its unregulated parent company, CMS Energy Corporation, the $1.2 to $1.5 billion payment it received for the worthless assets. When corporate affiliates transfer assets between themselves at inflated prices for improper advantage, the Commission's function

In the case of MCV alone, hundreds of millions of dollars of excessive electricity costs result from the Commission's acceptance of the utility affiliate's formalistic statements without investigating the substance of the intercorporate relationships or the underlying economics of the transactions involved. By not looking at the underlying substance—even where a state agency and a state appellate court had found the existence of a harmful, non-arm's-length, affiliate relationship—the Commission approved a scheme which invites further abuses. The Commission's approach improperly disregarded the $400 million to $1.2 billion of additional MCV profits transferred to Consumers Power through Consumers Power's sale of worthless assets to MCV for $1.2 to $1.5 billion. When those additional MCV profits are added to Consumers Power's acknowledged 49% share of all remaining MCV profits, there can be no doubt that Consumers Power's total share of MCV profits (i.e., its actual ownership share) exceeds even the Commission's lenient ceiling of 50%. *See* 18 C.F.R. § 292.206(b).

The Federal Power Act, as amended by PURPA, and companion Michigan statutes instruct the Federal Energy Regulatory Commission and the Michigan Public Service Commission to regulate rates in accordance with just and reasonable, cost-based ratemaking standards. 16 U.S.C. § 824a-3(b) (1988); 16 U.S.C. §§ 824d, 824e; Mich. Comp. Laws 460.557. PURPA was designed to encourage the entry of *non*-utilities into the business of building power plants. *FERC v. Mississippi*, 456 U.S. 742, 750-51 (1982); *Puerto Rico Elec. Power Auth. v. FERC*, 848 F.2d 243, 249 (D.C. Cir. 1988). PURPA specifically provided that only facilities that are "owned by a person not primarily engaged in the generation or

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is not to just look away. It is to prevent an avoidance of regulation required under the Federal Power Act and state statutes, namely that rates be just and reasonable. 16 U.S.C. §§ 824d, 824e (1988); Mich. Comp. Laws 460.557 (1991). In addition, the Commission's orders are contrary to PURPA's requirement that qualifying facilities not be owned by utilities. 16 U.S.C. § 796(18)(B)(ii).

sale of electric power" qualify for the special PURPA rates and for exemption from certain federal and state regulations. 16 U.S.C. § 796(18)(B)(ii); 18 C.F.R. §§ 292.601, 292.602 (1993). The Federal Energy Regulatory Commission's orders fail to take into account the anti-competitive consequences of expanding the availability of the PURPA exemption to utility affiliates such as MCV. Thus, a pro-competitive statute designed to encourage non-utility market entrants is turned into a mechanism to effectively deregulate utility-owned and controlled power plants. The result creates incentives for utilities not to deal with truly independent power plant developers and instead to favor their own affiliates in order to maintain economic dominance and to generate excessive profits that increase rates.

If the Commission's orders are not reversed, the public —including the millions of people represented by the member municipalities of the Michigan Municipal League —will suffer not only from hundreds of millions of dollars in excessive electricity costs, but from an intolerable regulatory structure: deregulation plus disincentives to competition. Electricity rates are too important to Michigan's economy, and to the nation's economy, to permit such a result.

CONCLUSION

The Petition for Certiorari should be granted.

Respectfully submitted,

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